

Tax Update: Understanding Real Estate Transaction Tax

October 2020

Summary

On 1 October 2020, Royal Decree A84 was issued announcing the creation of a new Real Estate Transaction Tax (RETT) with a rate of 5% calculated on the value of the real estate transaction. All real estate transactions that take place after 4 October 2020 will be exempted from Value Added Tax (VAT) and subject to the new RETT. This decision marks an effort to boost the real estate sector, which forms an integral part of the Kingdom's Vision 2030.

I. Understanding RETT

Who will administer RETT?

The General Authority for Zakat and Tax (GAZT) will be responsible for managing and collecting the new tax and the Minister of Finance will decide which VAT regulations will apply to the new tax until new policies and regulations are drafted.

Which transactions are subject to RETT?

The transactions subject to this new tax include transfer of ownership; the sale of commercial, residential, or agricultural real estate; and the sale of developed and undeveloped land. RETT is levied on all individuals and organizations involved in real estate disposals including natural and legal persons, corporations, companies and government agencies. There is no registration threshold for RETT, where all transactions are taxable except those exempted (see the section below).

The legal transactions subject to this tax include transfer of ownership, gifting, sale, inheritance, financial leasing, long term usufruct contracts exceeding 50 years, lease to own, and Islamic Murabahah.

Exemptions

- i. The transfer of real estate by inheritance.
- ii. The disposal of property as a gift to a spouse or to relatives to the second degree of affinity.
- iii. The disposal of properties as part of a legitimate will
- iv. Free transfer of property to licensed non-profit organizations and endowments
- v. Disposal of property to a government agency, to public corporate persons, or to entities and projects of public interest
- vi. Compulsory disposals of real estate (e.g. seizure of ownership for public benefit)
- vii. The sale of real estate to foreign governments, international organizations, and diplomatic missions accredited by the Kingdom
- viii. The disposal of property as a dividend in kind in joint stock companies (the stocks should not be disposed of for 5 years)

- i. The temporary transfer of property for use as a financial or credit guarantee
- ii. Temporary transfer of property between a fund and its trustee, the trustee and the fund, or the trustees of the same fund
- iii. The transfer of ownership of a property previously purchased under a financial lease or closed end lease where the date of agreement precedes 4 October 2020
- iv. The disposal of properties previously subjected to full VAT deduction provided that no change occurs to the parties of the transaction, the contract, or the clauses of the contracts subjected to VAT.

Value subject to RETT?

The transaction value agreed upon between the real estate vendor and buyer which should not be less than market value. The tax amount due should be settled before or during the real estate supply by the vendor, who would collect this tax from the buyer.

When is RETT due?

RETT is transactional tax where each transaction is registered via the GAZT portal without the need to apply for registration to GAZT. The obligation to register and submit returns for Zakat and other taxes do not apply to RETT.

RETT should be declared and paid for each transaction before or during the process of conveyance authentication by the competent authorities, or before or during the processing of disposals as authenticated by the competent authorities.

The declaration of RETT is mandatory even in the case of exemption. The competent authority will not process conveyance until RETT is paid or proof of exemption is provided.

Who should declare RETT?

The party applying for conveyance or authentication of disposal to a buyer must access the e-service on the GAZT website before starting official conveyance procedures at the Ministry of Justice or the Economic Cities Authority, or before or during the processing of the authentication between applicant and the buyer.

If the applicant's information indicates an exemption from RETT, GAZT will issue a notification and a reference number indicating the exemption. This reference number will be used to process the conveyance at the competent authority (i.e. the Ministry of Justice or the Economic Cities Authority). If tax is due, GAZT will issue a SADAD invoice for the tax amount to be paid.

Who should pay RETT?

The seller or disposer of the property is the applicant for the RETT e-service to whom a SADAD invoice will be issued according to information in the application for the tax amount due on authentication of the conveyance.

The seller may agree with the buyer on the extent to which the tax will be shared. Any of the parties to the transaction can pay the SADAD invoice, but the seller remains responsible for the payment of RETT and any tax due to GAZT. The buyer and seller are jointly responsible for all tax liabilities, therefore, GAZT has the right to interact with them individually or jointly.

Non-compliance

The issued amount should be paid within the deadline to avoid a penalty of 2-5% of the value of the unpaid tax for every 30-day delay. The assessment penalty due for non-compliance is equal to the tax amount with a minimum of 10,000 SAR. In case of tax evasion, the penalty will range between the amount of tax due and up to three times the value of the owed tax.

II. Interactions with VAT

VAT on goods and services related to real estate supplies

Construction costs will remain subject to VAT at a rate of 15%. In general, the input VAT paid on the construction costs will not be deductible, but licensed real estate developers will be entitled to recover such VAT subject to GAZT's approval.

In respect of current developments, the input VAT incurred on goods and services (construction costs) supplied to a taxable person and related to real estate transactions remains deductible provided that:

- the supply of goods and services occurred prior to 4 October 2020;
- the taxable person deducts the input VAT in its tax returns by 31 December 2020; and
- the proportional deduction of input VAT is applied where appropriate.

VAT registration for real estate suppliers

Persons engaged in the business of supplying real estate which is now exempt from VAT, and who have no other taxable business exceeding the registration threshold for VAT (SAR 375, 000), will be deregistered for VAT. Such person may remain registered voluntarily if required.

Purchase of a first home by Saudi citizens

In support of the Kingdom's citizens, the recent decision includes a commitment from the government to bear the RETT due for the purchase by Saudi Nationals of a first home up to a value of SAR 1 million, an increase on the previous value subject to VAT relief of SAR 850,000.

In such a cases, the citizen must provide the developer with a certificate of exemption from the Ministry of Housing (MoH). The real estate developer will declare and pay the tax due on the full value of the transaction and submit a claim for a refund of the tax to the MoH based on the citizen's certificate.

III. Other implications

All persons and entities involved in real estate transactions must consider the potential implications of the new tax on their activities. Since the RETT and the respective VAT changes took effect from 4 October, it is crucial that those affected gain an understanding of the application of the new regulations to their real estate transactions.

Some of the issues that will need to be addressed:

- The deductibility of input VAT when expenditure is used for supplies that are:
 - exempt from RETT;
 - subject to RETT (i.e. commercial and residential sale);
 - exempt from VAT; and
 - subject to VAT (i.e. commercial rent).
- The calculation of the tax base for RETT in the absence of a sale contract in the case of a gift or donation for other than relatives;
- Ongoing sale contracts where the suppliers have already charged and accounted for VAT;
- Transactions involving the transfer of ownership or possession of real estate is not yet completed (including transfers of economic activities, merger and acquisition activities); and
- The conditions to be met by the real estate developer to be classified as eligible to claim the input VAT on transactions subject to RETT;
- The impact of the new tax on the value of capital assets and thus on their depreciation; and
- The impact of RETT on the funding requirements for capital acquisitions of property.

Our teams are available to discuss these developments and assess their impact on your business.

Get in touch

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